

INTERNAL REVENUE SERVICE

DEPARTMENT OF THE TREASURY

District
Director

MAY 23 1989

[REDACTED]
Eiu: [REDACTED]
Person to Contact: [REDACTED]
Contact Telephone Number: [REDACTED]
Refer Reply to: [REDACTED]

Gentlemen:

We have considered your application for exemption from Federal income tax as an organization described in Section 501(c)(7) of the Internal Revenue Code.

The information submitted indicates that you were incorporated on [REDACTED] under the laws of the State of [REDACTED] and you were organized pursuant to the General Nonprofit Corporation Law of the State of [REDACTED].

Your purposes, as stated in Article II of your Articles of Incorporation, are to acquire, own and operate real property and building facilities for social, pleasure and recreational purposes; and to provide the facilities for social and recreational purposes of the general members of the association.

You state that [REDACTED] was originally owned by [REDACTED], and used as recreational lease land with each lessee owning his own cabin. In [REDACTED] the lessees purchased the land and formed [REDACTED]. On [REDACTED], the [REDACTED] County zoning Administration had issued a conditional use permit for the property to [REDACTED] on condition that the property could not be subdivided; that only [REDACTED] cabins would be permitted; that a county approved water system must be provided for all residents on the property; and proper road access to and from all inhabited lots must be provided. All work was to be completed within one year's time from [REDACTED].

At this time you have certificate holders (members) representing [REDACTED] cabins and [REDACTED] parcels of land. [REDACTED] parcels are vacant. Each cabin is privately owned while the parcel of land on which it sits is owned collectively by [REDACTED]. Each owner is responsible for the upkeep of his cabin and lot grounds. Each cabin may be sold for what ever price the owner can get. The new owner must pay a \$[REDACTED] certificate fee to the association to establish membership.

Your Bylaws stipulate that full time residency is limited to [REDACTED] cabins at any one time. The remaining cabins may not be used more than [REDACTED] months out of a year. New additions may be added to a cabin by submitting a plan or drawing to the association's Board of Directors for approval. Buildings are restricted to a single story with maximum square footage not to exceed 1,000 square feet for the entire structure.

████████████████████

In response to our letter of ██████████, you said the Association owns and maintains the roads and water system in the tract (photographs of which were submitted), and funds for upkeep and maintenance are raised by an annual assessment of the membership. The roads provide access to members' cabins; the water system serves all the cabins. You also stated that the Association expended money for tree maintenance for safety purposes.

Over the past ██████ years receipts of your organization were primarily (████%) derived from assessments of members for upkeep and maintenance of association property as provided in your bylaws. █████% of your receipts derived from interest income on checking and/or savings accounts. It appears that less than █████% of your expenditures can be directly related to group social activities (these occur under the heading "picnic supplies") while not even █████% of your income derived from group recreational activities ("picnic sales").

Section 501(c)(7) of the Internal Revenue Code provides that clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes are exempt from Federal income tax provided no part of the net earnings inures to the benefit of any private shareholder.

Section 1.501(c)(7)-1(a) of the Income Tax regulations provides that a club otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of club facilities or in connection with club activities.

Section 1.501(c)(7)-1(b) of the regulations provides that a club which engage in business is not organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes and is not exempt under section 501(a) of the Code.

It appears your club is engaging in business activities similar to those of the organization discussed in Revenue Ruling 68-168, 1968-1 C.B. 269, which leased building lots to its members on a long term basis. Its revenues, as in your case, were not raised from members' use of recreational facilities or in connection with the organization's planned or sponsored recreational activities. As it appears to be in your case, its revenues were primarily used to acquire, improve and maintain its properties. Subdividing and leasing of lots as described in the Revenue Ruling constitutes engaging in a business activity. Accordingly, exemption was denied.

In Revenue Ruling 75-494 1975-2 C.B. 214, the Service held that a club providing social and recreational facilities, whose membership is limited to homeowners of a housing development will be precluded from qualifying for exemption under section 501(c)(7) of the Code by owning and maintaining residential streets, enforcing restrictive covenants, or providing residential fire and police protection and trash collection service.

[REDACTED]

Your Association owns and maintains roads which provide access to your members' cabins. Your bylaws state your policy of restricting the size, height and appearance of members' cabins which is in effect the enforcement of restrictive covenants as noted in the Revenue Ruling above. Your Association provides water service to your members' cabins' which is a similar activity to providing trash collection, fire and police protection, and other services which are not social or recreational in nature.

A club may provide these services in connection with the maintenance and security of its social facilities. However, as soon as these services go beyond merely maintaining social facilities and begin to include services to residential areas, they are no longer exclusively in furtherance of pleasure and recreation. A club providing such services to residential areas will not qualify for exemption under section 501(c)(7) of the Code. Likewise, a club which enforces covenants for the preservation of the architecture and appearance of homes, is not operated exclusively for pleasure and recreation, and does not qualify for exemption under section 501(c)(7).

Your bylaws state that members have an annual meeting, but they do not indicate the existence of any recreational or social committees. However, they do forbid the keeping and riding of horses on Association property. Horseback riding is usually considered to be a recreational activity.

In our letter of [REDACTED], we asked how often your members get together and participate in social and recreational activities. You responded, in your letter of [REDACTED], "once a year, annual Memorial Day potluck picnic, some years we have a Christmas party for members. This included a breakfast, gift exchange and bowling. We have a few barbecues during the summer."

In Revenue Ruling 70-31 1970-1 C.B. 132, a flying club providing economical flying facilities for its members but having no organized social and recreation program did not qualify for exemption under section 501(c)(7). As the Revenue Ruling stated, a commingling of members must play a material part in the activities of a social club. Passive association is not enough.

Based on the information you have submitted, there does not appear to be any significant commingling of your members in structured, regularly carried on recreational or social activities. Any social and recreational programs operated by your organization are not evident in the financial records you submitted and are peripheral at best.

Since you are organized and operated in part to acquire and manage improved and unimproved lands; to perform the functions of a homeowners' association; to perform the functions of an architectural committee enforcing restrictions and conditions as well as to furnish, maintain and regulate common facilities and services for the benefit of your members, it is apparent that you are not organized and operated for the purposes specified in section 501(c)(7) of the Code.

Furthermore, you have not demonstrated that you have a regular program of social and recreational activities in which your members actively participate and commingle. Personal contact and fellowship are central to the concept of a social club.

Therefore, based on the material you have submitted, we hold that you are not entitled to exemption from Federal income tax as an organization described in section 501(c)(7) of the Code. You are required to file income tax returns annually with your district director.

You have indicated your agreement to our conclusion by signing and returning the agreement For 6018.

Sincerely yours,

District Director

Enclosures:
Form 6018